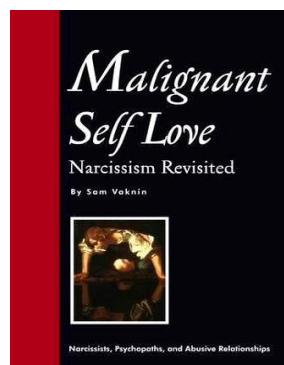


# *The Exporters' Pocketbook* *September 1999*

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## *I. The Export Transaction and Its Documents*

### **The Transaction**

- Finding a market for the goods (market research)
- Selecting the marketing channels
- Negotiations

- Pricing
- Distribution channels
- Order
- Contract
- Commercial Invoice

**Commercial Invoice must include (minimum):**

- Payment Terms
- Mode of Payment
- Division of Costs
- Details of Carrier
- Details of Receiving Party
- Details of Buyer
- Other Details

For best results use the ECE (Economic Commission for Europe) Standard Commercial Invoice

**Packing List must include (minimum):**

- Contents of the Packaging (=of the shipment)
- If more than one package or outer and inner packing – all contents per each packing and per each package must be detailed separately
- Permits and Licenses
- Export licenses if needed
- Standards certificates
- Labeling
- Quality control certificates (highest is ISO, such as ISO-9002 or ISO-9000)
- Health and phytosanitary certificates
- Veterinary certificates
- Other permits, licenses and certificates
- Service Providers
- Marine Transport
- Air Transport
- Land Transport (lorry, train)
- Insurance
- Warehousing
- Banking and other Financial Services (factoring, forfeiting, etc.)
- Airway Bill of Lading (ABL)
- (More details later – see appendices for samples)
- Holder of ABL does not own goods
- Air Transport Contract not effected – but ABL proof of existence of such contract, including weight, measurements, number of packages and invoice.
- Marine Bill of Lading (MBL)

- Proof of receipt of goods in a certain condition
- Proof of existence of transport contract
- MBL facilitates the transfer of ownership

Negotiable, transferable and assignable

**Subject to the Hague conditions and MUST INCLUDE:**

- Name and address of sender
- Port of loading and Port of discharge
- Date of lading and place of issuance of bill of lading
- Name of vessel and number of voyage
- Identity marks of cargo
- Description of goods – number of packing units, weight, volume
- Condition of goods – statement of carrier (if not stated – the goods are in good condition)
- "Clean on Board" not "Foul"

**Types of Bills of Lading (BL)**

- Shipped BL – Goods are on deck of ship
- Received for Shipment – Prior to loading onto ship
- Direct BL – From origin to destination, transshipment not allowed
- Ocean Through BL – In case of transit involving a few carriers. In such a case, each carrier imposes its own conditions on each leg of the voyage and for the limited duration it handles the cargo.
- Pure Through BL – First carrier must transport from port of loading to a mid-point and is responsible for damages to the goods.
- Combined Transport BL – Pure BL which covers shipment by all means of transport (sea, air, land).
- Forwarder BL – An agent's BL. Issued by an international forwarder.
- Freight Forwarder BL – BLs of the International Forwarders Association – FIATA

**Types of Insurance Policies (IP)**

The IP is prepared by the insurance agent or the insurance company.

- Open Time IP – One time IP, used in air/marine transport. Policy expires with the completion of the transport (with delivery).
- Open IP – Open or current policy used to insure a number of shipments. Payment of premium only for actual shipments. Entails a declaration by the insured to the insurer pertaining to each and every shipment on a pre-determined basis (ad hoc, weekly, monthly and so on).

The rights of the insured party are NOT effected if it BONA FIDE forgot or had no time to declare to the insurer as per above, or if it gave the insurer a declaration containing wrong information. The right declaration can be filed even after the goods are lost or delivered.

### **Types of Certificates of Origin (CO)**

Required by the authorities as a basis for customs duties and taxes discounts or exemptions under trade agreements.

Some destination require CO per each shipment. Others require CO only for specific goods. Sometimes the buyer demands a CO.

The exporter sends the CO to the buyer separately or with the goods.

Issued by the Chamber of Commerce, or by the Customs, or by the exporter itself or by its forwarder in trust.

- EUR1 – To the European Union
- FORM A – To the USA / NAFTA (the customs union of the USA, Canada and Mexico)
- CO

Warehouse Receipt proves warehousing of goods in the port area. Needed prior to commencement of the release of the goods by the customs.

- Orders
- Inquiry
- Indication / Quotation
- Order
- Firm Order
- Acceptance (the order becomes a contract by accepting it)
- Revolving Orders are considered contracts

Order through an agent – identical to order issued directly by a buyer (Important: demand from the agent proof of agency or representation, such as a power of attorney)

### **Should include:**

1. Price of Goods (including price ex factory, shipment / transport – freight costs, insurance, port taxes and expenses, other taxes, customs costs, forwarding costs, costs of issuing certificates, permits and licenses)

**IMPORTANT:** Make sure WHO pays WHAT

2. Specifications of Goods – Type of goods, quality, packing, number of units / quantity per package, packing sub-units

IMPORTANT: Prepare a sample for the buyer – which will be WORSE than actually delivered goods.

3. Quantity and Delivery Terms

If it is an on-going (revolving) order – get from the buyer a projection of its purchases in the future.

**TIME OF DELIVERY IS CRITICAL !!!**

4. Mode and Method of Payment

### **Transaction Documents**

- Documents demanded by the authorities (permits, licenses, standards and quality certificates, veterinary certificates, health certificates, labeling, etc.)
- Transaction documents (bill of lading, certificate of origin, commercial invoice and specifications, port and customs clearances, banking documents, etc.)
- Packing, Freight and Insurance
- Define outer and inner packing and sub-packing (materials, shape, size)
- Quantities
- Measurements
- Quality

IMPORTANT – Get freight offers from a few forwarders/carriers and make sure ALL the components are included in the price quoted!!!

Remember:

All costs, including the insurance premiums, are negotiable.

USE an insurance agent or an insurance expert within your company. Insurance is a complicated subject and the insurance companies do their best not to pay on claims.

### **Proforma Invoice (PI)**

Is actually an order and constructed as a commercial invoice –

But a commercial invoice **MUST** be provided separately.

Seller sends PI in duplicate (=2 copies)

Buyer signs one copy and returns it to seller

Buyer can prepare order or PI on its letterhead and send it to seller

Must include mode of payment

## **Sale Contract**

Use in case of a complicated transaction, the provision of services (or of goods which contain a service element – for example, maintenance or training)

## **Sole Distributorship Contract**

In case of doubt, use the ICC (international Chamber of Commerce) Model Contract (see appendix).

A distributor **BUYS** the goods and distributes them through a network of sub-distributors. He participates in advertising, marketing and sale promotion of the products he distributes. In return, he gets exclusivity for a certain territory, for a prescribed period of time and under certain terms and conditions. He does not distribute competing products and he uses a brandname.

An agent get a commission on sales generated through him – but does **NOT** buy the goods.

The Sole Distributorship contract **MUST** include:

- Definition of territory and products
- Commitment to act bona fide and with best efforts
- Roles of the distributor
- Non competition clause
- Distributorship and distribution channels
- Fairs, exhibitions, advertising, marketing and sales promotion
- Delivery terms and retail price list
- Sales plan and minimum sales obligations
- Sub-distributors and agents
- Information exchange
- Prices to distributor (distributor price list)
- Sales outside the territory
- Brandnames and Trademarks – protection and allowed usage
- Inventories and spare parts levels, maintenance and service
- Exclusivity
- Direct sales (by the supplier in the territory of the distributor)
- Updates and upgrades
- Validity and Expiry of the contract

- Termination of the contract
- Compensation for damages in case of early termination of the contract
- Obligation to return documents and inventory to supplier in case of termination of the contract

### **Agency Contract**

In case of doubt, use the ICC Model Contract (see appendix).

A Del Credere Agent undertakes to compensate the producer / manufacturer if the buyers (clients) default.

MUST include as a minimum:

- Appointment of the agent by the seller
- First right of refusal regarding new products
- Exclusion of OEM (sale to a third party which rebrands the goods with his own brand)
- Type of clients the agent may sell to
- Exact geographical definition of the territory
- Exclusivity (or lack of it)
- Bona fide collaboration and commercial fairness
- The roles and functions of the agent
- Endorsement and adoption of orders concluded by the agent with buyers
- No competition clause
- Marketing, advertising, fairs and exhibitions
- Minimal sales targets
- Sub-agency
- Obligation to exchange information
- Financial arrangements (Del Credere, other)
- Trademarks and brandnames
- Complaints of clients and buyers
- Right of seller to sell directly in territory of the agent
- Special clients / buyers
- Fees and commissions and formulas for their calculation
- Right of seller to reject business
- Expiry or termination date or absence thereof
- Survival clauses and unfinished business in case of termination of the contract

## ***II. The Process of Exporting***

## **Generalized Process of Export**

Order received

Letter of Credit or other payment document opened

Production and pre-export phases

Preparation of documents (EUR1, FORM A, specified invoice, licenses and permits, certificates of origin, etc.)

Instructions to forwarder and customs agent

Checking the prices of freight, insurance and forwarding

Commercial export (at the port facilities or customs terminal)

Receipt of documents (bill of lading, confirmed certificate of origin, etc.)

Presentation of documents at the bank and their transfer to the buyer's bank

Payment received

## **The Phases of the Export Process:**

Phase A – Decision

Phase B – Preparations

Phase C – Performance

Phase D – Post shipment

### ***Phase A – DECISION***

Collect Information (internet, specialized databases, market research, meetings, travel, fairs and so on)

Proforma Invoice

Production, quantity, quality, delivery terms, licensing

Price offer (firm offer)

Sale or Supply Contract



## **MAKE SURE THAT ...**

You are allowed to export the goods (no export restrictions on your goods)

Is there credit available for purchasing imported and domestically produced raw materials and parts – going into your exported goods?

Can you honour the order? Do you have sufficient capacity, the right manpower, the needed financing? It is better to say no than to renege on a contract.

### ***Phase B – PREPARATIONS***

Import of raw materials / parts (imported or foreign inputs)

Purchase of imported raw materials / parts in the local markets (domestic or local inputs)

Financing the imports

Financing the production

Production

Preparation of documentation

Engaging customs agents and international forwarders

Insurance

Quality certification

Export license

Freight and transport arrangements

Certificate of origin

Consular confirmation

### ***Phase C – PERFORMANCE***

Forwarding instructions to the customs agent

Packing

Withdrawal by customs agent

Preparation of invoice and specifications

Preparation of VAT claimback

Inspection of exported goods by authorities

Warehousing at the port

Custom clearance

Inspection of exported goods by the client

Port clearance

Authorization to load

Loading and release of documents

Receipt of bill of lading

Receipt of confirmed certificate of origin

Receipt of other documents

### ***Phase D – Post Shipment***

Financing the documents (=receiving payment)

Presentation of documents in local bank

Statistical registration

Tax and port tax rebates (in some countries)

### **Pricing the Exported Goods**

**Fixed Costs (Overhead)** – Administration, rent, accounting, amortization / depreciation, etc. Should be divided by man-hours or product units to determine their contribution to the costs.

**PLUS**

**Variable Costs** – Directly related to the production process. Wages, raw materials, fuel, etc. Increases with increased production.

**Incoterms Costs** – See Incoterms hereunder

Transporting the goods from factory to export port or terminal

Shipping the goods from export port or terminal to import port or terminal

Transporting the goods from import port or terminal to buyer.

### ***III. Incoterms***

#### **Incoterms**

Last determined by the ICC in 1994. There is also a 1936 American version.

Used by all parties to an international trade transaction: buyer, seller, banks, financial institutions, agents, forwarders, insurance companies, carriers, government authorities, lawyers and courts.

**See Appendix for detailed analyses of all 13 Incoterms**

**EXW** (Ex Works) – Seller provides goods in his factory yard. Buyer is responsible for all the rest, including loading the goods onto trucks in the seller's yards. Best to add: "loaded upon departing vehicle".

**FCA** (Free Carrier) – Seller provides export licenses, customs clearances and port documents to first carrier (determined by buyer) in an agreed location within the export country. Useful for MultiModal Transport (MMT) in land, air, or sea. Seller pays all port and customs inspection expenses. Seller's responsibility ends with delivery to carrier. Buyer pays all expenses from point of delivery (transport, insurance, special inspections).

**FAS** (Free Alongside Ship) – Seller delivers goods to a loading quay, alongside a ship, in an agreed port in export country. Buyer obliged to clear goods for export after having received loading documents from seller. Buyer pays all port expenses and expenses related to required documentation. Use only for marine freight.

**FOB** (Free On Board) – Seller delivers customs-cleared goods with bill of lading, export license, all taxes and duties paid clean (unharmed) on board a vessel. Seller pays all expenses until goods are clean on board. Buyer determines carrier and

pays the carriage (including loading expenses if part of the transport costs). Marine freight only. Best to add: "stowed and trimmed".

**Buyer must insure itself when using an "F" Incoterm.**

**CFR** (Cost and Freight) – Seller pays all expenses and transport costs to port of discharge. But responsibility for damage or loss or additional expenses is buyer's after goods loaded and stowed under deck. Seller obtains customs and port clearances, licenses, contracts with the carrier and with the insurance company regarding transport of goods to the point of loading. Buyer must obtain the import licenses, release the goods in port of discharge, issue insurance and pay for transit and inspection of goods. Marine freight only.

**CIF** (Cost, Insurance, Freight) – Seller arranges marine freight insurance for buyer and provides buyer with valid insurance policy in addition to obligations under **CFR**. Unless otherwise agreed, seller buys a limited "C" policy. Best to add: "free out". **It is important to mention the type of insurance and coverage sought by buyer.**

**CPT** (Carriage Paid To) – Similar to CFR but when MMT involved (car, train, ship and then airplane, for instance). Instead of On Board – use First Carrier.

**CIP** (Carriage and Insurance Paid To) – Similar to CIF but when MMT is involved. Responsibility reverts to buyer when goods delivered to First Carrier.

**DAF** (Delivered At Frontier) – Seller to deliver export cleared goods at a precise point at the border of either import or export country. Buyer obliged to clear goods through customs terminal, to obtain import license and to bear all import related duties, fees and charges. Seller must inform buyer ETD (Expected Time of Delivery) and precise location of delivery.

If preceded by international marine or air transport, point of delivery will follow the Main Carriage (used in train transport).

**DES** (Delivered Ex Ship) – Marine freight only. Seller must deliver export cleared goods to buyer on board a ship in port of discharge but has no responsibility to clear the goods for import in the destination country, to unload them and to ship them to final destination within the buyer's country.

**DEQ** (Delivered Ex Quay) – Marine freight only. Seller must deliver goods buyer outside the quay after unloading them from the ship and clearing them for import through port authorities and customs. Seller pays import taxes and port expenses. Seller must provide buyer with bill of lading and gate pass. Buyer must transport goods to his yards and if he does not must pay demurrage and warehousing.

**DDU** (Delivered Duty Unpaid) – Seller must deliver goods to buyer in a location within the destination country but buyer must clear them for import through the port and customs authorities. Buyers must pay all taxes and expenses related to the clearance.

**DDP** (Delivered Duty Paid) – Seller must deliver goods directly to buyer's location (or to any other address) after having fully cleared them for import and fully paid all taxes and expenditures related to such clearance. Best to add: "DDP-VAT unpaid" in case seller does not agree to pay the VAT.

### **IMPORTANT!!!**

The buyer and the seller must include all special conditions, not covered by the Incoterms – in their sale contract or order or commercial invoice.

Even if you include an Incoterm in a contract it is advised, to remove doubt, to also include a detailed list of rights obligations of the parties (=an agreed interpretation of the Incoterm). Always mention the version of Incoterms used (for instance: "FOB – Incoterms 1990").

The transfer of responsibility to the goods from seller to buyer does NOT constitute a transfer of title (ownership) to the goods.

There are Exit Contracts (seller delivers to buyer's carrier in country of origin of the goods and such a delivery ends the seller's responsibility) – All the Incoterms which start with the letters E, F and C. For example: CIF does NOT mean that the seller is responsible to deliver the goods in a port in the destination country – only that it has to pay for the voyage and for the insurance.

There are Delivery Contracts (seller delivers to buyer in country of destination and is responsible to them until they are delivered there) – All the Incoterms, which start with the letter D.

### **Insurance**

This is why insurance is critical (policy types A, B, or C).

It must include:

- Location in which the policy becomes valid
- Location at which the policy expires
- Extensions to the basic policy
- Political risks
- Value of coverage and types of coverage (replacement value, damages, etc.)
- Insurance of loss of profits
- The policy's currency

- Currency hedging

## **Important**

The buyer must provide full specifications of packing of goods

If the parties use a C Incoterm, the buyer is usually responsible for costs associated with an inspection of the goods by the authorities of the country of origin (**PSI** – Pre Shipment Inspection). If the buyer demands an inspection (quality and quantity controls) – it must be stated clearly who will bear the cost. If not specified – the buyer shall bear it.

It is recommended to use FCA when goods are not delivered to the carrier on quay or on board. Buyer must arrange the transport and provide the seller with exact instructions.

**"FOB Airport"** should not be used. FOB is ONLY for marine transportation. For air transport use FCA.

## **Incoterms in conjunction with Bill of Lading (BL)**

When CIF or CFR is used, use "on board BL" (goods have been loaded on board ship).

If goods shipped in containers, carrier may issue "Received for Shipment" (when he receives the goods and prior to their loading on board) – instead of BL.

It is preferable to use CPT or CIP if BL not required to conclude the transaction.

If goods arrive prior to original BL – they are delivered to buyer against a bank guarantee. Avoid it as it negates the function of the BL.

## **Non Negotiable Waybills and Receipts**

If a waybill is non-negotiable, there is no need to present its original to obtain delivery of the goods.

The following are non-negotiable:

- Liner Waybill
- Ocean Waybill
- Data Freight Receipt
- Cargo Key Receipt
- Sea Waybill

All air waybills are non-negotiable. Only the seller can instruct the carrier (not the buyer or his bank). Importers dislike non-negotiable waybills (unless explicitly stated that they are irrevocable). The names of the parties in the waybill must be irrevocable – otherwise, the seller can change them.

## **BLs, Receipts and Waybills**

Let us call all waybills and receipts – as well as bills of lading – transport documents (TD).

TDs are delivered to the buyer or to the seller according to instructions given to the carrier (never mind who paid for the carriage). The seller might get them to prove delivery. The buyer needs them to release the goods (to instruct the carrier).

TDs can be divisible (article A8 of Incoterms) in case one TD covers goods deliverable to many buyers.

Buyers responsible to release the goods and accept delivery – or to compensate seller for any damages.

Buyer is liable for damages to the goods after the transfer of responsibility from seller to buyer ("**Price Risk**").

It is recommended to use "Force Majeure" articles in sales contracts.

Some countries oblige exporters and importers to insure the goods in their own countries (to minimize foreign exchange outlays).

## **Rules of Use of Incoterms**

1. Use **DEQ, DES, CIF, FOB** and **FAS** only in marine carriage and for marine freight.
2. Use **CPT, CIP, FCA** universally except if goods are in bulk of carried in chartered vessels.
3. Be clear: how are the goods to be transported, who has the obligation to have them loaded, who pays for what, who is responsible to clear the goods, to release them and to unload them and so on.
4. Be clear: how much insurance you require and what type (**A, B, C**)
5. What restrictions and special demands would you like to impose on the carriage and the carrier.
6. Include "**Force Majeure**" and validity, expiry and termination clauses
7. Indicate which Incoterms version is used (example: FOB-Incoterms 1990).
8. The Incoterms **CPT, CIP, CFR** and **CIF** deal only with the transport aspect of the transaction – not with the transfer of responsibility or ownership.

## ***IV. Payment***

### **Payment**

Payments schedule (when?)

Payment mode or method of payment (how?)

Place of payment (where?)

Currency of payment (which?)

### **Payments Forms**

Advance payments (cash in advance)

Open account credit

Cash Against Documents (**CAD**)

Documents for collection, Cash on Delivery (**COD**)

Letter of Credit or Documentary Credit (**L/C**)

### **General Principles of Payment**

If cash was paid in advance by buyer, seller will give buyer the documents, courier them to the buyer or airmail them (Captain Mail them).

COD – the carrier delivers the good against cash (collect).

But in all other forms of payment:

The carrier of the goods is hired by either the seller or the buyer to carry the goods, in accordance with instructions, to a destination.

The seller sends the goods to a bank in geographical proximity to the final destination of the goods.

The transport documents (bill of lading, waybill, receipt) are sent to that **CONSIGNEE** bank.

The consignee bank – having received the transport documents, the commercial invoice, the certificate of origin, the insurance policy and other documents, invites the buyer to buy (to redeem) these documents (with which he can get the goods).



The buyer pays the bank and the bank endorses the bill of lading and instructs the carrier (if the BL is non-negotiable) to give the goods to the buyer.

The buyer pays the carrier, presents the endorsed bill of lading and gets a delivery order with which the buyers releases the goods, having paid customs, duties, taxes and port expenses. He receives a gate pass which allows him to load the goods to his lorries and transport them to his yards.

## **Open Account**

Either with big, reliable clients, or with agents, distributors, subsidiaries which maintain a consignment warehouse or a forward warehouse.

Use **Exchange Note** – A financial instrument in which the seller instructs the buyer to pay his bank for the goods. The buyer signs the note. Buyer's signature confirms receipt of the goods in good order and the buyer's debt. Exchange notes are transferable, negotiable, endoreseable and assignable.

It is a stand-alone document which does not refer to the underlying transaction.

It is recommended to date the exchange note (on its back) and thus transform it into a **Time Note**.

## **Cash On Delivery (COD)**

Payment with delivery of goods.

Exporters which maintain warehouses in destination countries – use COD.

Payment can be in cash, deposit receipt, bank guarantee, bankers' acceptance.

Be careful to receive payment only by your authorized representative.

## **Cash Against Documents**

1. Contract
2. Carriage of goods to port of discharge
3. Documents (commercial invoice, bill of lading, insurance policy, certificate of origin) transferred by to seller's bank for collection
4. Seller's bank (usually through carrier) transfers documents to buyer's bank
5. Buyer's bank (the consignee) invites buyer to receive endorsed (ownership transferred to buyer) documents
6. Buyer deposits payment (or arranges credit line) for the goods in his bank
7. Goods delivered to buyer (using the endorsed documents)
8. Buyer's bank transfers the payment to seller's bank

9. Seller's bank credits seller's account with the payment minus fees and charges and commissions

If bank endorses documents to buyer prior to receipt of payment – the bank assumes the buyer's obligation to pay.

**CAD not to be used with branded or customized goods** (buyer might refuse the goods and if they are branded or customized – they cannot be sold to another buyer).

### **Banker's or Bank's Acceptance (Accept)**

Exporter can ask buyer to provide a bank draft. An acceptance stamp and signature on the draft ("Accept") transforms it into an obligation of the bank itself to pay, on a given date to bearer.

Both Exchange Notes and Bankers' Acceptances are traded in special exchanges in the world.

### **Letter of Credit and Documentary Credit**

A letter in which a bank undertakes to pay the exporter if and when the exporter meets certain terms and conditions enumerated within the L/C.

The bank's commitment is usually irrevocable (the L/C should contain this word: "irrevocable" – although it is irrevocable even by default).

If the exporter fulfils all the conditions of the L/C - the bank will pay, regardless of the situation of the buyer. If the seller did not comply with the conditions in the L/C, the bank will pay only if buyer expressly agrees to it.

### **IMPORTANT**

1. The letter of credit is only as good as the issuing bank
2. Check: are the conditions of the L/C identical to the conditions specified in the sale contract, the commercial invoice or the order?

### **UCP-500**

These are the uniform rules of international payments determined by the ICC in Paris, France:

1. Importer signs sales contract which includes prices, schedules of delivery and payment, types of packing, modes of carriage, volume, documents to be exchanged and more. Importer gets pro-forma invoice from exporter.

2. Based on the pro-forma invoice, Importer asks his bank to open letter of credit in favor of Exporter. Importer instructs the opening bank which details to add to the L/C which are not included in the Sales Contract or in the pro-forma invoice. Such details may include: permission or prohibition of transit, transshipment, division of the L/C, part shipment, the number of copies of the documents, certificates of origin, the coverage amount of the insurance policy, should the policy be endorsed and so on.
3. The bank uses its letter of credit form and incorporate all the terms and conditions of the sales contract in the letter of credit.
4. The Importer's bank send the details of the L/C to the Exporter's bank (the Correspondent Bank).
5. The Correspondent Bank informs the Exporter that an L/C was opened in the Exporter's favor and conveys to the Exporter the details of the L/C.
6. Exporter compares the conditions of the L/C to the conditions of the sales contract and especially whether the Importer's Bank has irrevocably agreed to accept the Correspondent Bank's signature regarding the receipt of the documents.
7. Exporter consults his bank and others whether the Importer's bank is a prime, world bank of good standing.
8. Exporter makes sure the L/C is valid and corresponds to the timetables agreed with the Importer regarding both the delivery of the goods and payments. Another question: can the documents be negotiated or transferred within the term of the L/C? Can the Exporter accept all the restrictions and limitations of the L/C? Are there any impossible conditions (for instance, in contravention of the foreign exchange regime) or wrong details (name of a port which does not exist, etc.).
9. If the L/C is accepted by the Exporter, he starts production and manufacturing operations. When the goods are ready, Exporter contacts a carrier. After the goods are loaded, Exporter gets a bill of lading, a certificate of origin EUR1 or FORM A signed by the Customs, an export list and other documents.
10. Exporter presents documents to his bank which checks whether all required documents have been presented and whether they comply with the conditions of the L/C. The correspondent bank then issues an **ACCEPTANCE**. The L/C then becomes a bank guarantee.
11. If the correspondent bank is also the confirming bank, it also pays the Exporter.
12. The correspondent bank transfers the documents and the acceptance to the opening bank.
13. The opening bank checks the documents. But if the correspondent bank is also the confirming bank – even if the documents are wrong or faulty – the opening bank must pay.
14. The opening bank transfers the payment to the correspondent and confirming bank.

15. The opening bank informs the Importer that the documents arrived. Importer deposits payment with the opening bank (or opens a credit line with it).
16. Importer gets from the opening bank the documents endorsed.
17. Importer clears the goods and takes delivery of them through the carrier (he gets a **delivery order** from the carrier, having settled all outstanding accounts with carrier).

### **Settlement by Acceptance**

1. Seller transfers documents to correspondent bank with a note made out to the bank (the bank is the note's beneficiary).
2. Correspondent bank confirms acceptance of dated note to the seller.
3. Opening bank gets the document.
4. Opening bank credits correspondent bank.

### **Settlement by Negotiation**

1. Seller transfers documents to correspondent bank with a note made out to the buyer (the buyer is the beneficiary of the note).
2. The correspondent bank pays seller against documents and note.
3. Correspondent bank transfers documents and note to opening bank.
4. Opening bank credits correspondent bank.

### **Letters of Credit - Form, Structure and Details**

1. Number and ID (this number must be placed on all subsequent documentation pertaining to the same transaction).
2. Names and details of buyer, seller, opening bank (buyer's bank), correspondent bank.
3. Description of goods – usually the proforma invoice is attached and this sentence is then added: "In accordance with proforma invoice number ... dated ...herewith attached to this letter of credit and which constitutes an integral and inseparable part thereof".
4. Total cost or price.
5. A list of documents (with the presentation of which by the seller payment to the seller will be effected):
  - a. Commercial invoice, including a list of the goods, details of buyer and seller and signatures.
  - b. Packing list signed by seller.
  - c. Insurance policy including its type, the coverage it affords, amount covered. The policy's beneficiary must be the opening (importer's) bank and it must be fully endorseable.

- d. Detailed billways, receipts or bill of lading: who is entitled to receive delivery of the goods, who pays for the carriage, is carriage prepaid and where, etc.
  - e. Other documents.
6. Dates – when was the L/C opened, how long is it valid, date of loading and date of presentation of documents at the bank (maximum 21 days after loading of goods, if not otherwise specified).
  7. Special instructions: is transit or transshipment allowed (best to write "transshipment allowed"), is part shipment allowed (best to write "part shipment or partial shipment allowed").

If carriage or delivery not according to L/C – **L/C will NOT BE PAID!!!**

## **Types and Specifications of Documentary Credits**

### **Confirmed versus Unconfirmed**

Opening bank uses a bank in the Exporter's country (usually the correspondent bank) to interface with the exporter.

The corresponding bank informs exporter about opening of L/C and checks and verifies the exporter's documentation after goods have been loaded (such verification subject to opening bank's consent).

Sometimes the correspondent bank verifies the documents AND pays for them – this is known as **CONFIRMATION**. With a confirmed L/C, the correspondent bank must pay the exporter upon verification of the documents. The exporter pays a confirmation fee.

### **Transferable and Divisible**

An L/C that can be transferred to or be paid in parts to sub-contractors and suppliers of the Exporter. Only one transfer is allowed:

1. The name and details (address, etc.) of first beneficiary can be changed to name and details of second beneficiary.
2. The amount of transferred credit must be smaller than original amount of credit.
3. The period of validity of the L/C or its parts can be altered.
4. The percentage of insurance can be increased.
5. The details of the new L/Cs issued on basis of original L/C can be different to details of original L/C – as long as new L/C are less (in amount) or shorter (in period) or partial and do not expand the original L/C or otherwise enhance it.

## **Revolving**

For a series of identical transactions with known delivery and payment schedules.

If irrevocable, cannot be revoked even if revolving and even if the buyer went bankrupt. The bank is responsible to pay.

## **Counter Credit (Back to Back)**

The L/C is pledged by the Exporter to his bank (the corresponding bank) or (more often) to another bank against receipt of credit from the bank. This credit is then used to pay suppliers.

The exporter's obligation to pay the back to back credit it received from its bank – is NOT dependent upon the payment of the L/C used as a collateral.

## ***V. Shipping***

- a. Packing and transportation of goods to port or terminal
- b. Marine transport
- c. Air transport
- d. International forwarding and customs agency
- e. Cargo insurance
- f. Credit insurance
- g. Prevention of loss and damages
- h. Labeling
- i. Land export and import

## **Packing**

Cardboard (two or three waves)

Crate (wood with or without cardboard)

Wooden boxes (heavy and expensive)

Barrels (metal, plastic, wood; for the transportation of fluids; fluids must fit the material of the barrel)

Sacks (jute, paper, plastic, cloth)

**The Goods can be transported ...**

Loose (each unit – box, barrel, etc. – separately)

Unitizing (one unit composed of sub-units) – shrink, containers, big bags or semi bulk, stretch, etc.

## **Marine Transport**

The carriage fee or rate + charges, fees, levies, duties and commissions = carriage tariff

Influenced by:

### **Fixed and variable transport costs**

(such as the distance traveled, expenses and fees in various ports, balancing the cargo, frequency, size and type of vessel, properties of the goods, modes of loading and warehousing, volume/weight ratio, transport risks, possible damage to cargo, size of cargo and its composition, etc.)

But "Likes are not treated as likes" – different prices are quoted for similar situations.

This is because of additional costs related to the **market in the goods and to the marine transport marketplace**.

The carriage fee is determined also by "what the traffic can bear" – how in demand are the goods, how valuable they are, etc.

The conditions of the global marketplace in marine transport and the competition in it also determine the quoted price – as well as fees, levies, charges, commissions and taxes in the various ports and in the various origin and destination countries. Changes of technology also influence prices.

Tariffs are determined as **CLASS RATE** – a class of transport, which includes many types of cargo with the same rate or

**A COMMODITY RATE** – specifically tailored to every type of cargo and multiplied by the weight or the mass (volume). Payment is according to the higher of the weight and the mass.

To this the exporter should add charges (such as the **Heavy Lift Charge** or the **Extra Length Charge**) and other levies...

...such as the **CAF (Currency Adjustment Factor** – a currency hedge in favor of the shipowner);

...the **BAF (Bunker Adjustment Factor** – a percentage of the rate intended to offset certain expenses of the ship operator);

**War Risk (or Political Risk** – to offset a high insurance premium);

**Congestion Surcharge** (to offset expenses which are the result of long periods of waiting at the port) or

**THC (Terminal Handling Charges** – imposed by the port itself for the right to anchor).

### **Containers**

#### **Door to Door (House to House)**

An empty container is deposited with the exporter in a pre-determined date.

The Exporter fills it and transports it to the harbor.

In the destination country – the container is deposited with the importer.

He empties it, returns it to the port.

#### **Pier to House**

In the port of discharge, cargo and goods from different suppliers are concentrated in one container which is then sent to the importer / buyer.

#### **House to Pier**

Like House to House – but because the container contains goods for various buyers, the container itself is not sent to any single buyer.

#### **Pier to Pier**

Cargoes reach the port, get containerized by the agent in the port of loading. In the port of discharge, it is emptied and each cargo is sent separately to each buyer.

#### **Consolidation**

Transporting the cargoes of a few sellers in one container.

#### **REMEMBER !!!**

Compare Prices – you will always find a cheaper alternative!!!



## **Types of Ships**

**Liner** – operate in regular lines with regular vessels in pre-determined dates

**Charter(ed)** –

**Voyage Charter** – Cargo owner charters a vessel to transport the cargo from port of loading to port of unloading

**Time Charter** – Cargo owner or shipping company charters a vessel for a defined period of time (upto a few years)

**Bareboat Charter** – Long term (5-15 years) charter (common in the transport of fuel and grains). The lessee takes care of the cargo, of operating the vessel and its crew

**Container ships** – Built like a beehive with cells the size of containers

**RORO** – Cargo rolled on wheeled carriages under deck (for transporting vehicles, etc.)

## **Multi Purpose Boat**

**Tankers** (fluids, liquids, fuel)

**Bulk** – Transports grains or chemicals in bulk

**Lash** – Carry with them big platforms or rafts

## **Conference**

All shipowners are organized in a cartel called "Conference"

## **Marine Bill of Lading (MBL)**

Serves as a receipt for the cargo, proof of existence of a carriage contract and proof of ownership. It is negotiable and endorseable.

Under the Hague principles, a bill of lading (BL) must include the following:

- a. Name and address of shipper / exporter
- b. Port of loading and port of discharge
- c. Date of loading and place of issuance of BL
- d. Name of vessel (ocean liner, etc.) and voyage number

- e. Cargo identification marks
- f. Description of goods – number of units, weight, volume (mass)
- g. Condition of goods (if not filled – no external or visible damage)
- h. BL must be "clean on board" not "foul"

A Marine Bill of Lading must include these to be valid:

- a. The words "bill of lading" and the words "lading" or "shipped" (which prove that goods have been loaded on board vessel)
- b. Date of loading
- c. Confirmation of the shipping company
- d. Numbers of original bills of lading, if any
- e. The words "Clean on Board"
- f. Name of the shipper
- g. Name of the consignee or "To Order" (of the shipper) together with endorsement of the shipper
- h. Name of vessel
- i. Port of loading, final destination and is re-loading required
- j. Name of parties to be notified upon arrival to the port of discharge
- k. Marks and numbers stamped on the packages
- l. Abbreviated description of the goods (weight, number of units and volume / mass)
- m. How many original copies of the MBL are there and is the presentation of all original copies required in order to release the goods

### **Types of Marine Bills of Lading**

**Shipped MBL** – Goods were loaded and carrier received them in good order

**Direct MBL** – No transshipment allowed

**Ocean Through MBL** – Transit MBL. When more than one carrier handles the goods, each one is responsible for the goods only during his tenure and under the terms and conditions of his contract

**Pure Through MBL** – Pure transit MBL. The first carrier must transport the goods from the port of loading to the port of discharge through an intermediate port and is responsible for damages

**Combined Transport BL** – Covering all modes of transport (not only sea)

**Forwarder BL** – Issued by an agent, an international forwarder

**Freight Forwarder BL** – Issued by FIATA, the international organization of forwarders

## **IMPORTANT**

The Hague Principles regulate the legal relationship between carrier and shipper from loading to discharge.

It covers only exported goods, carried by vessels by sea

It applies only when a transport contract has been incorporated in the BL

It does not cover goods (such as animals) **on deck**

## **Air Transport**

### **Types of Transport Tariffs**

Air transport tariffs are indicated by IATA – but often these tariffs are ignored. SHOP AROUND.

**Minimum Rate** – not in accordance with actual weight (when under 45 kg.)

**General cargo Rate (GCR)** – for all kinds of cargo

**Specific Commodity Rate (SCR)** – per a minimum weight of a specific type of cargo and valid for a limited period of time. Cheaper than GCR.

**Unit Load Device (ULD)** – Special tariff for cargo transported as a unit on a surface or in a container. Only weight is limited (maximum and minimum)

The tariff is derived from:

1. Destination of cargo
2. Type of goods – SCRs can be negotiated with the local IATA representative
3. Minimum Rate
4. Weight / Mass (volume) ratio (every 6 cu.m. equal 1000 kg.) – if W/M exceeds this ratio – payment will be according to weight

## **REMEMBER**

Try to exceed the minimum rate and the minimum weight

Negotiate an SCR or a ULD wherever possible

Make sure that the W/M ration does not exceed the allowed ratio

## **Airway Bill**

Issued by the air carrier.

Mainly a confirmation of transport – not of ownership or any right to goods.

Absence of airway bill does not effect validity of contract of air carriage or the applicability of the treaty – but may prevent carrier from resorting to exemptions and other restrictions in the treaty.

Airway bill is proof of weight, measurements, quantity and packing. It is also a carriage invoice, an insurance policy (if insurance taken out by carrier) and a customs declaration (if no other declaration is required by law).

Not negotiable and ownership cannot be transferred by its endorsement or transfer.

Only consignee can accept delivery at discharge. Buyer appears under "also notify" when bank is consignee and fiduciary on behalf of seller. Buyer receives power of attorney from bank to release and clear the goods.

Issued in three original duplicates to shipper, consignee and carrier.

## **International Forwarding and Customs Agency**

The international organization of forwarders – FIATA – created a document system called **FBL (Forwarder's Bill of Lading)** - equivalent to MBL). The forwarder responsible for goods door to door (house to house).

**FCR (Forwarder's Certificate of Receipt)** – A receipt issued by forwarder confirming receipt of goods at the factory to be carried to destination.

**FWR (Forwarder's Warehouse Receipt)** – Receipt issued by forwarder that it received goods in a warehouse to be carried to destination.

**Airfreight Forwarder** – As opposed to marine forwarders, airfreight forwarders have to comply with certain professional and financial conditions. Some of them are IATA forwarders – with minimal volume of activity, proven acquaintance with airfreight rules, skilled staff and so on. IATA forwarders get 5% of carrier's rate and are allowed to issue airway bills to shippers on behalf of air carriers.

An airfreight forwarder:

Arranges a number of shipments, unites them and passes them to the aircraft, handles commercial export / import operations for exporter / importer, prepares all

paperwork, takes care of transit from one aircraft to another and of air insurance (if client demands it), consolidates cargoes, issues airway bills and selects routes.

**Customs Agent** deals with goods only within the port while an international forwarder handles the goods from door to door.

Customs Agent deals with the following:

Reserving space in a vessel, coordination of acceptance of containers, provision of information regarding prices, routes, schedules, preparation of documents for exporter including BL, CO and all other documents demanded by the customs. The agent appraises and classifies the goods for customs purposes, obtains a gate pass and arranges the transportation of the goods to the buyer's location.

The buyer is responsible for the activities of the agent.

### **Cargo Insurance**

About 0.15% of value of cargo, except if dangerous or fragile cargo.

**One Time Policy** expires with completion of transport.

**Open Policy or Current Policy** – see above.

### **REMEMBER**

Insurance is cheap – use it abundantly.

Insure the cost, the profit, the carriage rates, the marine insurance premium, port expenses and land transport, customs agency, import taxes and so on.

Double marine insurance is allowed.

Marine insurance is subject to the **London Clauses. Institute Cargo Clauses** deal with general cargo.

**A Clauses Coverage** – All risks insurance against loss or damage caused by random event which happens outside the cargo and affects it.

Does not cover loss or damage which is the result of intentional behaviour of the insured, general leakage, loss or vaporization of mass or weight, normal wear and tear, inappropriate packing or preparation of insured goods, breach of contractual schedules and obligations by insured or owners, charterers or operators of vessel, inherent defects, war, nuclear fusion or fission, radioactive material, incapacitation of vessel known to insured at time of loading.

**B Clauses Coverage** – loss or damage due to fire, explosion, shipwreck, capsizing, derailment of a land vehicle, collision or contact with another body except water, unloading in distress, earthquake, volcanic eruption or thunder, general average, penetration of sea, lake, or river water into the ship's warehouses, lift, etc., total loss of cargo which fell in the sea during unloading or loading.

**C Clauses Coverage** – covers only catastrophic marine disasters such as fire, explosion, shipwreck, drowning, capsizing, derailment, collision, unloading in distress, general average or dumping in the sea.

### **Credit Insurance**

Both private and state companies (such as ECGD in the United Kingdom, COFACE in France and OPIC in the USA) provide insurance:

- Against the credit risks of the buyer
- Against political risks (war, terror, acts of state)
- Against financial risks (non convertibility, non repatriation)

Credit risks insurance policy serves as collateral. It is pledged against credit, which goes towards financing the production of the goods and working capital.

Credit insurance firms check and rate clients (or rely on credit rating agencies such as Moody's, Fitch-IBCA for banks or Dun and Bradstreet). They issue policies guaranteeing payment to the supplier / exporter in case of the buyer's bankruptcy, refusal to pay, default, nationalization and expropriation, etc.

Insurance is provided mainly or only to firms registered in the domicile of the insurance company or in another member of the same customs union or trade block (EU, EFTA, etc.) – so, it is recommended to establish subsidiaries in these territories to be eligible.

Premiums range between 0.5-0.7% per insurance unit for a period of 90 days.

### **Prevention of Loss and Damage**

Use only new packings suitable to the goods

Fit crates and cardboard boxes with metal corners

Use shrink wherever possible, tie and strengthen everything massively

Do not paste labels with descriptions, pictures, brandnames, trademarks or labels on the packages – these attract thieves. Mark the packing with letters and numbers on at least two of its sides. Proper packing is an implied warranty in the carriage contract and an expressed warranty in a marine/ air insurance policy.

Mark the packages with instructions: "Fragile", "Printed", "Handle with Care", "Avoid X-rays" and so on.

The standard marking of cargo should include:

1. Initials or abbreviated name of consignee (full name and address required in case of road or rail transport)
2. Reference number (order number or similar). Avoid indicating the date
3. Name of port and final destination and "via" in case of transit
4. Package number out of total (example: 2/20)
5. Mark the packages Big, Clear and Brief (BCB)
6. Use metal, plastic or strong cloth tags – do not use cardboard or wood tags
7. Marks bags and sacks with sealing liquid
8. Mark dangerous and radioactive materials with warnings, the chemical composition and the shipper's name
9. Use Latin letters as well as local alphabets – a maximum of 10 lines of 17 characters each
10. It is advisable – but not required – to mark gross weight in case of air transport. Net weight and measurements are not required at all – unless chemicals or dangerous materials are involved.
11. Some countries demand to mark the name of country of origin, number of import license, etc. – pay attention to local regulations

Change your markings often.

Use big packages to pack smaller and non-uniform packages in.

Leave no empty space inside the package – fill empty spaces with paper, Styrofoam, pad the goods and tie them tightly.

Do not overfill the crates, sacks, or boxes.

Do not concentrate the goods in one part of the package (internally) – spread them evenly.

Place light cargo on heavy cargo.

Separate types of packings (cardboard boxes from crates, etc.)

Do not leave any space between the wall of the container and the packaged goods.

## ***VI. More on Documents***

## **Invoice**

Must include:

- Country of Origin
- Place and date of preparation, number of invoice, reference to order number
- Names, addresses and other details of buyer and seller (and consignee if not the buyer), address for delivery of documents
- Type of carriage (sea, land, air, multimodal)
- Port of loading
- Port of discharge
- Final destination
- Commercial conditions and schedules (delivery and payment)
- Number of packages, their description and markings (numbers, etc.), statistical classification
- Description of goods according to type, quality, special properties, composition in percentages of each material
- Amount of goods in units / weight / volume
- Gross, net and net net and measurements of each package
- The price agreed between the parties, costs of freight and insurance
- Conditions of shipment, dispatch and payment, including all discounts, fees, commissions and charges
- Exporter number if any
- Stamp and signature of seller plus declaration that all the above is true

## **Packing List (Specifications)**

The first part includes name of firm, date, address of buyer and, sometimes name of bank, payment conditions, etc.

The second part contains very detailed description of the goods and their packing. Some countries demand the inclusion of special units of weights and measurements, method of marking, customs classification and so on.

## **Insurance Policy**

Includes the value of the goods, details regarding the mode(s) of transport, points of departure and arrival, details of the agency or insurance company to be contacted in the destination country in case of damage.

Must include the following details to be valid:

- Name of insurer
- Policy number



- Details of carrier
- Route from exit to entry
- Total value insured and type of currency
- Conditions of the policy
- Details of agent in destination country
- Jurisdiction in case of disputes
- Description of goods and their packing
- Date of issuance of insurance
- Method of calculation of the premium (marine insurance, war surcharge, registration, policy, credit if payment of premium is post dated)

## **Bill of Lading**

Contains description of goods, their quantity and quality ("clean on board" or "foul").

Airway bills include an invoice to be paid by buyer or seller.

If seller pays, the bill will say "prepaid" – if buyer is to pay, it will say "collect".

In case of marine bill of lading, a detailed invoice is issued to seller.

## **Certificate of Origin**

### **EUR1**

Issued at the request of the buyer.

Confirmed by the chamber of commerce, the customs, or the exporter or his agent / forwarder – or any other body authorized by them.

Must be printed without corrections.

Must conform to commercial invoice.

Must include:

- Name and full address of exporter
- Name and full address of consignee
- Description of goods and their packing
- Weight of goods in kg. Or volume in liters
- Numbers of relevant invoices
- Declaration of exporter that goods conform to rules of origin stipulated in the agreement under which the certificate of origin is issued

## **FORM A**

Like EUR1 but:

- Authorities do not need to confirm it
- The percentage / amount of value added of the goods must be declared (or "P" in case the goods are also produced in the destination country)

### **Consular Confirmation or Consular Invoice**

Demanded mainly by developing countries.

Includes full description of goods in language of destination country – including quantities, monetary values and a sworn affidavit of the exporter attesting to the veracity of the data.

## ***APPENDIX I: The World of the Internet***

### **First Steps**

Buy a computer – including modem, graphic card with 2Mb buffer and multimedia (sound card, speakers)

Open an account with one of the internet service providers – ISPs (PTT, Unet, MOL, or others)

You will get:

- a. An installation software on a diskette (usually someone will come to install it for you)
- b. A username (which is also the name of your account and part of your email address)
- c. A password – keep this secret and change it often
- d. Certain ISPs will give you a separate password for communication purposes

### **Let's Go Surfing**

Click on the phone (connection) icon – a window will open

Type in your password and click with the left button of the mouse "OK"

Once connected to the network (you will be informed by a separate window which will show you the status of your modem and how much time you are connected) – you have opened the door to the world of the internet

The internet is like a huge city with many "addresses" of "sites". To visit these sites, you need to have their addresses (which usually start with [http://](http://members.tripod.com/~samvak/guide.html) - example: <http://members.tripod.com/~samvak/guide.html>)

You also need a "car" to take you to the sites – a special software called "browser". The two best known are Microsoft Internet Explorer 5.0 and Netscape Communicator 4.61. In this demonstration we will use the Explorer because it is user friendly.

Click on the browser icon and study the browser. You can always click on the "Help" button to get detailed help.

To visit a site you can either:

- Click on the address if it is active (in blue color in a computer file), OR
- Copy the address (mark it, click the right button of the mouse and click copy in the menu)
- Click "file" in the browser toolbar, then click "open" (or click the "open" button of the browser directly)
- Paste the address that you copied (click the right button of the mouse and click paste in the menu)
- Click "open"

The browser will find the site whose address you asked for and bring you there.

Once in a site, you can click on any COLOURED (hyperlinked) text to visit other sites.

## **Search Engines**

But what if you don't have the address?

In other words, how do you find an address of a site? Or, even more difficult, how do you find sites which deal with subjects you are interested in?

To do that, you need to use "Search Engines". These are special software applications. Look at the list of addresses you received under the heading "search engines". You have there the addresses of the 6 most important search engines.

Let us exercise.

You are interested to find the addresses of tobacco organizations in the United States. You have no idea which sites deal with this subject, let alone what are their addresses.

Open the "Alta Vista" search engine (or any other – the biggest are Alta Vista and Northern Light, the best organized are LookSmart and Yahoo) – using the address you have.

Type your search term: "tobacco organizations in USA" (use the "" marks).

You will get a list of sites.

Click on the colored text (the hyperlinked text).

Each title you click on will lead you to another site.

We will learn more advanced modes of searching in this seminar.

The internet is the biggest library in the world. It has everything you need about any subject in the world. BUT, it is very chaotic.

### **Other Ways of Knowing Things**

A more orderly way of obtaining information is by:

Subscribing to specialized providers of information through subscription databases – such as DIALOG and NEXIS-LEXIS (let's find their addresses through the internet)

OR

Subscribing to specialty magazines and CD-ROMs (let's find a few of these through the internet) – the biggest such providers are US agencies (the USDA and even ...the CIA!!!).

### **Electronic Mail (E-Mail)**

When you open an account with an ISP – you get an email address. This is YOUR address in cyberspace, in the world of the internet. It is NOT the address of a SITE – it is your PERSONAL address and it looks like this: [sand@mpt.com.mk](mailto:sand@mpt.com.mk) (all letters usually small).

You can:

- Send messages
- Receive messages
- Send and receive computer files (attached to the message as attachments) – whole documents, pictures, diagrams, faxes, EVERYTHING and you can send it at the price of a local phone call to anywhere in the world.
- Design a special signature

Good luck and welcome to the internet.

## ***Appendix II: Incoterms In-Depth***

### **Documentary Credits and INCOTERMS - International Commercial Terms**

1. Incoterms are part of international sales contracts. They regulate:
  - A. Carriage of goods from seller to buyer
  - B. Export and import clearances
  - C. Division of costs and risks between the parties
2. Important acronyms: Electronic Data Interchange (EDI), Electronic Data Interchange for Administration Commerce and Transport (EDIFACT) and Uniform Rules of Conduct for Interchange of Trade Data by Teletransmission (UNCID).

Internet: GE - TPN

3. Electronic Bills of Lading – use the CMI Uniform Rules.
  4. As a result of the container revolution and cargo unitization, the incoterms FCA, CIP and CPT were developed. Emphasis shifted from means of conveyance to the place of carriage. FOR / FOT / FOBA were omitted.
  5. Case Study: warehouse to warehouse insurance and the FOB point - where is delivery effected?
- CIF - seller exposed to claims for failing to reach the ships rail on time.
6. The mirror method - the 10 headings – see Appendix of Incoterms.
  7. INCOTERMS - part of larger picture (deal with delivery and with nothing after delivery - not with quantity, costs of loading / discharging, clearance, transport, risks of loss / damage and insurance against them, title, quality breach of contract or price). There are: Contract of sale, applicable law, custom of trade.
- Example: an FOB Buyer would insure the goods despite the fact that Incoterms do not oblige him to do so - difference between obligation and commonsense.
8. Specific reference required. Example: trading with a US firm (UCC - AFDT).

9. CISG - Contracts for the International Sale of Goods: POD where breach is determined in conjunction with Incoterms (concerning delivery).
10. D-terms: seller's delivery obligation is extended to the country of destination (arrival contract).
- E-terms, F-terms, C-terms: seller fulfils delivery obligation in his country (shipment contract).
11. The common error: there is no connection between risks, costs and delivery.
12. F-terms: Free of risks
- C-terms: Costs borne after critical risk point reached
- D-terms: Destination
- C-TERMS: 2 points of interest: delivery and risk / costs
13. FCA buyer to instruct seller how to hand over goods – and wher  
FCL Full loads (railway wagon / container) vs. LCL break bulk
14. FOB additional service
- Seller contracts for carriage - though he has no obligation to do so
15. FOB The port decides how to distribute loading
16. FAS Seller does not have the obligation to clear goods for exports (unlike FOB!)
17. C-terms Do not stipulate arrival date! seller obliged to ship good  
so that they COULD ARRIVE!
18. CFR, CIF Only by sea! A8 demands bill of lading / sea waybill  
If Buyer wants to sell in transit - he will be unable because of lack of  
the right document ⇒ breach of seller
19. CIF, CIP Minimum Cover vs. all risk and political

### ***Appendix III: More about Modes of Payment***

**SIGHT DRAFT (=COD) - Document against payment**

- Original shipping document attached --> CB (collecting bank)
- Original bill of lading made to the order of the shipper and endorsed by him blank, or to the order of CB
- Notification to drawer of draft about payment

### **TIME DRAFT**

- Like sight drafts but paid X days after acceptance
- The CB holds and presents for payment

**BANK GUARANTEE** dependent on underlying obligation or independent (=note)

- Bid bonds } dependent
- Performance bonds } dependent
- Advance Payment bonds } dependent
- Payment Bonds } independent but with recourse and stoppable by court injunction

### **LOCs**

DLC - Documentary

FLC - Financial

SLC - Standby

- CLEAN (Self-contained)
- REGULAR (Dependent on an event)

### **FACTORING AND FORFAIT / EMC**

COLLECTION

CREDIT PROTECTION

FINANCING (=LOAN / Credit line) on Approved Accounts

Recourse Factoring: Collection + Financing

How to choose a Factor?

### **Profile of Users of Factoring**

Restricted access to credit

High or low net worth

Satisfied customers

Credit - worthy customers

Successful products / services

### **Factoring Services**

Conventional Min 2 ½ %, 3 days (5% per 30 day invoice)

Weekly agings, daily collection reports

Credit services, fees prorated daily,

2-weekly reserve releases, 24 hour funding

No hidden fees / long term contracts

Debt Consolidation Payment to creditors when company is in default

Maturity On pre-approved account debtors

Financing / Sale - Leaseback (for bankrupt companies) including equipment

### **How does It Work**

Bring invoice + delivery slip

Receive upto 80% of the face amount

Receive the balance (reserve) when the invoice is paid

## ***Appendix IV: International Trade – An Introduction***

1. **Globalisation** - economic interdependence of nations.
2. **Imported products** = imported employment = internal unemployment



### 3. **Ricardo's theory of Comparative Advantage**

4. **Absolute advantage** - fewer resources to produce the same products

**Comparative Advantage** - it takes less to produce the same in terms of other goods

### 5. **Two country / two goods model - mutual absolute advantages**

#### **Phase A: Mutual absolute advantage**

Macedonia USA

Wine 6 2

Tobacco 2 6

#### **Phase B: Land allocation for equal unit production**

Macedonia USA Totals

Wine  $25 \times 6 = 150$   $75 \times 2 = 150$  300

Tobacco  $75 \times 2 = 150$   $25 \times 6 = 150$  300

#### **Phase C: International trading**

Macedonia USA Totals

Wine  $100 \times 6 = 600$  0 600  
(Mac. sells 300 to USA)

Tobacco 0  $100 \times 6 = 600$  600  
(USA sells 300 to Mac.)

7. **Trade** enables countries to **move beyond** previous resource and productivity constraints.

### 8. **Two country / two goods model - unilateral absolute advantages**

#### **Phase A:**

Macedonia USA Totals

Wine  $50 \times 6 = 300$   $75 \times 1 = 75$  375

Tobacco  $50 \times 6 = 300$   $25 \times 3 = 75$  375

## **Phase B: Land allocation for equal unit production**

### **Macedonia USA Totals**

Wine  $75 \times 6 = 450$  0 450  
(Mac. sells 100 to USA)

Tobacco  $25 \times 6 = 150$   $100 \times 3 = 300$  450  
(USA sells 200 to Mac.)

9. **Explanation:** The **opportunity cost** of 3 bales of **tobacco** in **Macedonia** is 3 litres of **wine** - in **USA**, only 1 liter.

The **opportunity cost** of 1 litre of **wine** in **Macedonia** is 1 bale of **tobacco** - and in the **USA** it is 3 **bales**.

10. When countries **specialize** in production of goods in which they have a **comparative advantage** - they **maximize** their **combined output** and **allocate** their **resources** more **efficiently**.

11. **Terms of trade:** The **ratio** at which a country can trade domestic products for imported ones.

**In the above example:** 1 litre **wine** = 2 bales **tobacco**

**Macedonia** benefits because its opportunity cost is  $1 = 1$

(it would get 1 bale domestically by giving up 1 litre)

**USA** benefits because its opportunity cost is  $1 = 3$

(it would have to give up 3 bales domestically to get 1 litre)

12. **Exchange rates** determine the terms of trade.

For any pair of countries, there is a **range of exchange rates** which can lead to both countries **realizing gains from specialization and comparative advantage**.

Within that range, the exchange rate will **determine which country gains the most** from trade.

13. **Two country /two good world**

### **Macedonia USA**

Wine 3 DM \$ 1

Tobacco 4 DM \$ 2

Exchange rate Price of DM Result

\$ 1 = 1 DM \$ 1 Macedonia imports both

\$ 1 = 2 DM \$ 0.5 Macedonia imports wine

\$ 1 = 2.1 DM \$ 0.48 Macedonia imports wine -

\$ 1 = 2.9 DM \$ 0.34 USA imports tobacco

\$ 1 = 3.3 DM \$ 0.33 USA imports tobacco

\$ 1 = 4 DM \$ 0.25 USA imports both

14. **Comparative advantage** can be expressed in **terms of exchange rates**:

Instead of comparing goods directly - money is used.

In Macedonia - the production of 1 bale of tobacco costs 4/3 litres of wine.

15. **Exchanges rates** in the right ranges **drive countries to shift resources** into sectors in which they enjoy **comparative advantages**.

16. **Factor endowments** - the **quantity** of labour, land and natural resources of a country

17. **Heckscher - Ohlin theorem and the Learner corollary**

A country has a comparative advantage in the production of a product if that country is relatively well endowed with inputs (natural resources, knowledge capital, physical capital, land, skilled and unskilled labour) used intensively in the production of that product.

18. Why do countries **import and export the same product?**

**Differentiation** of products in response to diverse preferences / brand loyalty.

19. **Acquired (versus natural) comparative advantages** (specific skills, goodwill)

## ***PROTECTIONISM***

1. **Protection** - shielding a sector of the economy from (foreign) competition

2. **Tariff** - tax on imports

**Export subsidy** - payment to encourage exports

**Dumping** - sale of products at prices below the costs of production

**Quota** - limit on quantity of imports

(mandatory and legislated or voluntary and negotiated)

3. **GATT, the Uruguay round, the WTO, latest multilateral WTO agreements**

4. **Free trade zones: EU, NAFTA, MERCOSUR, FTA (economic integration)**

5. **Trade barriers**

**Prevent** a country from **benefiting from specialization**

**Push** it do adopt **inefficient production techniques**

**Force** consumers to pay **higher prices for protected products**

6. **Protection Counter - Argument**

(A) **Saves jobs**

- Reallocation - **not disappearance**
- Retraining **and relocation**

(B) **Unfair trade practices**

**Underinvestment in environment**

(C) **Cheap foreign labour**

**Reflects lower productivity**

**(unfair competition)**

**This IS comparative advantage**

(D) **Protect national security**

**Every** industry uses it

(E) **Discouraging dependency**

(F) **Safeguarding infant industries**

**No infant industry asked for help** (allows them to acquire comparative advantage)

(H) Protection against currency fluctuations

**What is proper rate?**

**Temporary currency overvaluation**

## **International Trade and Exchange Rates**

1. International trade is determined by exchange rates.
2. History: The gold standard, Bretton Woods (1944-1971), the snake (EMS), the Louvre accord (1985).
3. Influences on foreign exchange: central banks interventions, macroeconomic policy, statements by policymakers.
4. Balance of payments: the record of a country's transactions in goods, services & assets - current account and capital account.
5.  $(\text{Merchandise exports} - \text{merchandise imports}) = \text{balance of trade (deficit or surplus)}$   
 $+ (\text{exports of services} - \text{imports of services}) = \text{net export / import of services}$   
 $+ (\text{income from investments}) - (\text{payments to investors}) = \text{net investment income}$   
 $+ \text{net transfer and other payments} = \text{current account}$
6.  $\text{Increase (-) or decrease (+) in private (and in Government) assets abroad} + \text{increase (+) or decrease (-) in foreign private (and in Government) assets in the country} = \text{balance of capital account}$
7.  $(6) + \text{statistical discrepancy} = \text{balance of payments}$
8. Debtor and creditor nations
9. The effect of a sustained increase in Government spending (or investment) on income (= the multiplier) - is smaller in an open economy, some of the extra consumption goes to imports.

Multiplier =  $1 / 1 - (MPC - MPM)$  (in open economy)

10. Anything that affects consumption - affect imports (income, aftertax real wages, aftertax nonlabour income, interest rates, relative prices and the state of the economy).

11. The trade feedback effect - export increases consumption which increases imports. Imports in one country is exports in another which increases consumption and so on.

An increase in one country's economic activity leads to worldwide increase in economic activity which feeds back to that country. Its imports stimulate other countries' exports which stimulate those countries' imports and so on.

12. Prices of exports / imports are influenced by inflation.

Export prices of other countries affect a country's import prices.

Inflation is exported through export. It affects a country's import prices.

13. An increase in the price of imports affects local prices:

(A) Through stagflation: rising prices and falling output

(B) Expensive imports lead to increased demand for domestic products

14. The price feedback effect

Inflation in one country is exported to another and then re-exported to the first

15. The demand and supply for currencies

Firms, households and Government that import / export

Tourists in / out the country

Buyers of stocks, bonds or other financial instruments in / out the country

Investors in / out the country

Speculators who bet with / against a currency

16. What affects appreciation and depreciation of currencies?

The law of one price (for the same good everywhere)

For the same basket of goods - The exchange rate would be determined by the relative price levels in the 2 countries

This is the purchasing power parity theory (PPP)

17. PPP does not account for transportation costs

Substitute products are not identical

Baskets of goods are different

18. Relative interest rates - higher rates lead to appreciation

19. Imports, like taxes and savings are a leakage from the income - consumption cycle.

Exports are like investments and Government purchases (stimulate output).

20. A depreciation stimulates exports and domestic consumption = the GDP

21. The J curve: balance of trade gets worse before its gets better following a currency depreciation.

Exports increase, imports decrease, currency price of exports doesn't change very much (until domestic prices adjust), currency price of imports increases.

The value of imports increases, even as volume decreases, initially.

22. Expansion of money supply ® decrease in interest rates ® investment and consumption ® lower inventories ® rising income (output).

Lower demand for debt securities ® lower demand for currency ® more foreign securities bought ® currency sold and depreciates ® stimulates the economy.

## ***Appendix V: Countertrade***

### **COUNTERTRADE - (A) GENERAL**

1. **Countertrade** - a transaction which links exports to imports in place of a financial settlement

2. **Reasons**

- A. Trade financing risky (debt crisis)
- B. Tight import credits (because of low exports)
- C. Entry into new markets (both the exporter and the importer)
- D. Products differentiation and creating competitive advantages
- E. Convertibility or political - financial problems

### **3. Transaction phases**

- A. Identify target country arrangements / regulations
- B. Evaluate their attractiveness and
- C. Find the most favored one from the buyer's perspective
- D. Match your strengths with current / potential countertrade (internal / external uses for the goods, distribution network)
- E. Consider the accounting / taxation aspects
- F. Choose between in - house expertise and outside specialists
- G. Beware of risks:
  - a. Quality and consistency of goods
  - b. Delivery times
  - c. Supplier reliability
  - d. Changes in the value of goods over time
  - e. Negative attitude of Governments and IFIs (e.g., EXIM bank in USA)

### **4. Countertrade is a marketing tool:**

- A. Generating hard currency for clients
- B. Helping them to market their products
- C. Sharing (information, marketing, technology, production)

### **5. Countertrade components**

- A. Piecing together sources of finance, services and supplies in different countries to minimize hard currency net outlays of the importer.
- B. Creating FOREX income for the importer through unrelated protects / new investments.
- C. Partial payment in soft currencies through reinvestment of the proceeds in the importer's country.
- D. Escrow accounts in foreign banks funded by the importer through export revenues (hedge until counter delivered goods are sold).

### **6. Arguments in favour of countertrade**

- A. International commerce - an extension of national (economic) policies.



- B. (Leads to) a preference to deal with trade competition through bilateral accommodations favoring domestic exporters.
- C. Uneven recovery rates and protective import policies.
- D. A hedge against declining trade levels.
- E. The growing third world debts.
- F. Constraints on credits and debt rescheduling.
- G. Dependence of developing countries on import - led growth and export expansion for debt servicing and unemployment.
- H. Tool of long term industrial policy and economic planning.

## 7. Factors affecting the future of countertrade

- A. Ability of world markets to accommodate counterdeliveries.
- B. Nature of assets offered (raw materials, components, finished goods).
- C. Streamlining of bureaucratic bottlenecks.
- D. Willingness of western exporters to engage in higher risk trade.

## COUNTERTRADE - (B) FORMS

1. **Countertrade and offset** are reciprocal arrangements.

Countertrade is the exchange of goods and services intended mainly to alleviate FOREX shortages of importers.

**Offset** is intended to advance industrial development objectives.

2. **Assets exchanged** include physical goods, services (e.g., tourism, engineering or transportation), rights (licenses, leases, etc.), lien instruments (e.g., sovereign promissory notes), or temporary ownership (BOT - built, operate, transfer arrangements).

3. **Developed industrialized countries** emphasize technology and production processes while **developing countries** emphasize additional exports.

4. The **contractual arrangements** include cashless exchange of goods of comparable value, parallel import / export transactions with their own separate finances, production sharing / equity position.

5. **Countertrade ratio** - percent of the value of export offset by counterdeliveries

DISAGGIO - subsidy paid as a commission / discount by the exporter to a broker responsible for marketing counterdeliveries (in the hands of the broker it is AGGIO).

**SWITCH** - transfer of rights to countertrade goods to third parties

Protocol / link or framework contracts - side agreement linking the primary and secondary contracts in a countertrade

## **6. Bilateral Government - To - Government trade agreements**

Reciprocal market access privileges (preferential terms)

- A. To integrate the economies using clearing units - exporters and domestic currency by their Central bank.
- B. Special political / regional trade relations.
- C. Trading interests for raw materials sources.

7. **SWING** - margin of credit allowed on a bilateral clearing account (beyond which all trading stops ) - usually 30%.

**Clearing SWITCH** - DISAGGIO driven financial operations. Bilateral imbalances are monetarised by brokerage networks through final sale products sourced from the country with the clearing arrears (or rights to products).

## **8. Forms of compensatory trade arrangements**

**OFFSET** - in cases of purchases of military / (high cost) civilian equipment, counter - purchases are demanded as compensation.

Usually in the form of expansion of industrial capacity: coproduction, licensed production, subcontracting, overseas investment, technology transfer, countertrade.

(IN) **DIRECT OFFSET** - articles (not) related to the sale.

**BARTER** - one time exchange of goods / services of equivalent value.

[examples: US - Jamaica, the dissolution of COMECON, Brokers' swaps]

**BUYBACK (Compensation)** - exporter receives products derived from the export.

Each leg is regulated by a separate contract.

**COUNTERPURCHASE** - exporter receives products unrelated to the export.

Exporter not allowed to transfer his credits and some advance purchases by exporters qualify.

**UMBRELLA (Countertrade agreement)** - includes multiple trading partners.

Between Western exporters and Government entity (**Evidence account**)

Between Governments concerning specific products (**Bilateral clearing**)

Countertrade used to release **blocked currencies / funds**

(Expatriation of profits against compensation)

**OFFSHORE ESCROW ACCOUNTS** - insulation from local banks ensure timely payments to exporters

Allowance for insufficient cash flows (production / marketing slippage)

## **COUNTERTRADE - (C) ANALYSIS AND PLANNING**

### **1. BENEFITS** (mainly intangible)

- A. Locking in foreign market shares
- B. Circumventing export restrictions
- C. Supporting subsidiaries /affiliates
- D. Depleting surplus inventory
- E. Preserving production / employment levels

### **2. COSTS** (mainly tangible)

- A. General and administrative (handling, documentation)
- B. Subsidy (DISAGGIO)
- C. Financing and insurance (including holding & escrow accounts)
- D. Performance / completion guarantees

### **3. RISKS**

- A. Expensive and partial insurance
  - B. Political risks and bureaucratic delays
  - C. Liability claims (personnel, product)
  - D. Property risks (direct damage or time dependent)
  - E. Lack of standardization
  - F. Shortfalls in delivery and marketing of the products
  - G. Losses due to delays: changes in production / export priorities
- sudden unavailability of raw materials

- crop failures
- inadequate transportation
- quality problems
- non-competitive pricing
- (arbitrary) marketing restrictions
- protectionist shifts
- contract failures of brokers / end users

#### **4. COUNTERMEASURES**

- A. Analysis and viable pricing (maybe inflation of export prices)
- B. The right contract
- C. An insurance policy
- D. Information about the importer, the markets and potential competitors  
brokers / end users
- E. Recognizing anticipatory purchases and additionality requirements  
(transferable)
- F. Separate the contracts to insulate performance and to facilitate financing,  
guarantees and insurance

#### **5. The CONTRACTS**

- A. Primary sale - standard export contract + countertrade clause
- B. Link contract - the countertrade contract includes:
  - 1. amount and period of obligation
  - 2. type, standards, pricing criteria of counterdeliveries
  - 3. names of companies providing counterdeliveries or: free  
choice clause
  - 4. transferability clause
  - 5. currency of payments
  - 6. notification and remittance procedures
  - 7. rights or restrictions affecting the marketing of goods
  - 8. non-performance penalties and damages
  - 9. disputes, termination, unavailability of goods
- C. Counterpurchase (buyback) contract includes:
  - 1. reference to primary contract
  - 2. standards, specifications, pricing, handling
  - 3. disputes, force majeure, arbitration, law, indemnities

### **COUNTERTRADE - (D) SUPPORT SERVICES**

1. **TRADING HOUSES** have:

- A. Specialists and experience
- B. Financial resources
- C. Positions in markets and / or marketing networks

Can help with:

- A. Marketing and representation
- B. Transportation, warehousing, insurance
- C. Finance: credits and investment management
- D. Manufacturing, upgrading

2. **BANKS** - advisory services and matchmaking, switch trading of clearing currencies and debt conversions

3. **INSURANCE** - state and private (LLOYDS, CHUBB, AIG)

4. **OTHERS** - law firms, trade consultants and information firms, export management companies, government agencies, industrial giants

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